Supreme Court, U.S.
FILED
NOV 10 1994
OFFICE OF THE CLERK

No. 94-708

In the Supreme Court

OF THE

United States

OCTOBER TERM, 1994

EL DORADO PALM SPRINGS, LTD.,
a California Limited Partnership,
DBA EL DORADO MOBILEHOME PARK,
Petitioner,

VS.

RENT REVIEW COMMISSION OF THE CITY OF PALM SPRINGS,
Respondent.

RESIDENTS OF EL DORADO MOBILEHOME PARK,
Real Party In Interest-Respondent.

BRIEF IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI TO THE CALIFORNIA COURT OF APPEAL FOURTH APPELLATE DISTRICT, DIVISION TWO

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I.

INTRODUCTION

The Petitioner, EL DORADO, has failed to adequately show that the California Supreme Court (denying review of the California Court of Appeals, Fourth Appellate District, Division Two)[1] decided an important question of Federal law which has not been, but should be, settled by this Court,

[1]See El Dorado's Petition for Writ of Certiorari, Appendices 1 and 5.

or has decided a Federal question in a way that conflicts with applicable decisions of this Court [*U. S. Supreme Court Rule 10.1(c)*]. Petitioner's principal reliance for a writ to issue is allegedly founded upon the "just compensation" clause of the *Fifth Amendment of the United States Constitution.*

The underlying statute applicable herein is the *Palm Springs Rent Control Ordinance* ("ORDINANCE") an initiative Ordinance originally approved by the voters of the City of Palm Springs in a General Municipal Election held on April 8, 1980. The Ordinance establishes the maximum rents that a mobilehome park owner may charge to the residents of a mobilehome park, utilizing Base Rents established prior to the imposition of the rent controls. Rents are automatically adjusted upwards on an annual basis in proportion to annual increases in the Consumer Price Index (CPI). In addition thereto, Landlords may request "hardship" rent increases whenever the Landlord can show and convince the Rent Review Commission that its Net Operating Income (NOI) is not being maintained on a level proportional to its Base Year's NOI. The NOI is also allowed to increase annually in proportion to the CPI increases. The Rent Control Ordinance, therefore, provides that the Landlord receives a "fair and reasonable" return by allowing rent increases to assure that the NOI is increased annually in proportion to the increase in the CPI.

Petitioner herein, EL DORADO, has benefitted by the application of the annual rental increases attributed to the annual increases in the CPI. It has also benefitted in increasing its NOI by the "hardship" rent increases granted by the COMMISSION and affirmed by the Courts of the State of California. Only after EL DORADO volitionally refinanced its debt structure (increasing such debt from $7,360,000 to $8,600,000) and failed to otherwise comply with the provisions of the Ordinance did EL DORADO cry

foul, and claim that it was deprived of "just compensation." As is described below, the facts in this instance do not support EL DORADO's claim for the issuance of a Writ of Certiorari.

II.

STATEMENT OF FACTS[2]

The following material facts were conveniently omitted from EL DORADO's Petition For Writ of Certiorari, and are stated hereinbelow to clearly show that EL DORADO was not (and is not presently) deprived of earning a "fair and reasonable" return on its investment; therefore, EL DORADO experiences no violation of the *Just Compensation Clause of the Fifth Amendment of the Constitution.* Furthermore, the full facts in this case show that EL DORADO was afforded its full due process rights in all proceedings before the Administrative Agencies ("COMMISSION") , and subsequently, before the Judicial Courts of the State of California.

A. THE LANDLORD'S (EL DORADO) REAL INVESTMENT IN THE SUBJECT PROPERTY.

EL DORADO purchased the mobilehome park ("SUBJECT PROPERTY") on April 1, 1986, for a total purchase price of $7,500,000. EL DORADO's investment consisted of a down payment of $140,000, plus two promissory notes: a purchase money mortgage of $5,400,000 and a secondary mortgage loan from the seller in the amount of $1,960,000. EL DORADO's investment was less than two percent (2%) of the purchase price — 98% was financed by way of the two

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[2]This "RESIDENTS' " Opposition Brief continues to identify the parties to this action as "EL DORADO," "COMMISSION," and "RESIDENTS" as more fully identified in the Petition for Writ of Certiorari (Article IV.A., pg. 3 of Petition).

purchase money mortgages.[3] The Landlord's (EL DORADO) *real investment* in the mobilehome park was a mere *$140,000.*

B. EL DORADO'S REQUESTS FOR "HARDSHIP" RENT INCREASE

On the very same day that EL DORADO closed escrow in purchasing the park, EL DORADO filed its request with the COMMISSION to increase rents in the approximate amount of *$180.00* per lot, per month in the 377-lot park.[4] EL DORADO believed that it found a "loop-hole" in the local Rent Control Ordinance. Said loop-hole concerned debt-servicing costs — mortgage interest payments considered as a necessary element of operating expenses. For every dollar increase in the debt-servicing costs, there would be a corresponding (proportional) increase in monthly rental fees. Upon recognizing the existence of the debt-service loop-hole provision in its rules and regulations, the COMMISSION immediately repealed said provision in December, 1986. The circulatory effect of such a provision (escalating debt costs) is the antithesis of the underlying provisions of rent control regulation.

Upon pursuing its "hardship" rent increase petition before the COMMISSION, the Trial Court, and the Court of Appeals of the State of California, EL DORADO was successful in obtaining the full amount of its "hardship" rent increase request.[5] The California Court of Appeals acknowl-

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[3]The financial data related to the purchase of the park was supplied by EL DORADO, and is supported by public recording records and is, therefore, uncontrovertible.

[4]An increase of rental income in the amount of $814,320.00 annually, a rental increase of over 70%.

[5]*El Dorado Palm Springs, Ltd. v. Rent Review Comm.* (1991) 230 Cal. App. 3d. 335, rev. denied, 1991 Cal. LEXIS 4091.

edged that EL DORADO had a *"vested right"* to include its debt service costs as an operating expense (when calculating its Net Operating Income — "NOI") because its existing purchase money financing was incurred *prior to* the repeal of the debt-service provisions (Rules & Regulations). However, the Court of Appeal also ruled that the former debt-servicing provision *would not apply* to any subsequent financing that occurred after the repeal of said provisions.

EL DORADO thus benefits from the consequences of the "loop-hole" provision in the Rules & Regulations of the COMMISSION (as such rules existed on April 1, 1986), and receives the benefits of the approximately $180.00 per month, per lot (377 lots) rental increase. As a net effect of such rental increase (while the original financing was in place) , EL DORADO enjoyed a Net Operating Income of approximately *$670,000* (after payment of all operating expenses, real property taxes, and debt-service costs of approximately $573,000). Considering EL DORADO's investment in this project ($140,000), the Net Operating Income (NOI) represented a return of over *470%* on its investment.

EL DORADO did *not* seek appeal of the above-referenced Court of Appeals decision.[6]

C. EL DORADO'S SUBSEQUENT REFINANCING OF ITS DEBT-MORTGAGES

In March, 1989, EL DORADO performed a 100% refinancing of its then existing mortgage-debt. It replaced its then existing debt (approximately $7,360,000) with a new promissory note in the amount of $8,600,000. Firstly, EL DORADO did not disclose to this honorable Court what it

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[6]id.

did with the excess cash resulting from the refinancing.[7] Secondly, EL DORADO gives *short shrift* to the specific ruling of the Court of Appeals of the State of California (see EL DORADO's Pet. for Writ, pg. 8, 2nd para.) on the subject regarding the refinancing act. When EL DORADO performed a 100% total refinancing of its existing debt structure, it vitiated all prior rights which were exclusively dependent upon the provisions which were repealed three (3) years earlier (December, 1986). EL DORADO appeared to believe, and relied upon such belief, that it could perpetually refinance its debt, and continue to extract rent increases from its tenants, without the debt ever being fully paid off.

D. EL DORADO'S ALLEGED OPERATING LOSSES ARE NOT IMMEDIATELY ATTRIBUTABLE TO THE DIRECT OPERATING EXPENSES OF THE PROPERTY.

EL DORADO's operating expenses subsequent to the refinancing of its debt structure (March, 1989) included the following expenses:[8]

	1989	1990	1991
Legal Expenses[9]	$261,483	$280,623	$260,923
Interest[10]	885,317	916,447	975,517
Depreciation[11]	348,511	344,778	323,945

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[7]EL DORADO apparently diverted the $1 million plus resulting from the refinancing to other purposes.

[8]As reported by EL DORADO in its tax returns, voluntarily submitted.

[9]Legal expenses in 1986 were $26,262, as reported by EL DORADO.

[10]Interest expenses consist primarily of mortgage debt servicing.

[11]Depreciation allocations resulting primarily from purchase costs, plus capital improvements.

EL DORADO laments that it has incurred substantial cash flow operating losses since purchasing the park in 1986. As is readily discernable from the above, EL DORADO, at its own initiative and volition, has increased its legal expenses by approximately *$240,000/year* (NOT for direct operating costs, but for legal pursuit of unconscionable rent increases). Likewise, as a direct consequence of its increased refinancing, it has incurred proportionally larger interest expenses. Its mortgage debt was increased by approximately 17% ($7.36 million to $8.6 million) resulting in an unusual and *unnecessary* increase in interest expense in the amount of approximately $150,000. Legal expenses and interest expenses alone account for approximately *$400,000/year* of unusual and unnecessary cash flow drain. EL DORADO has not suffered operating losses as a consequence of being deprived of its constitutional rights, but rather as a consequence of its own wrongful actions.

III.

FIFTH AMENDMENT — THE JUST COMPENSATION CLAUSE — A FAIR AND REASONABLE RETURN ON INVESTMENT STANDARD

The *Palm Springs Rent Control Ordinance* assures the Landlord a "fair and reasonable" return on its investment by employing the Maintenance of Net Operating Income ("MNOI") approach.[12] Utilizing this approach, and considering the uncontroverted financial data presented by EL DORADO, EL DORADO is assured that in 1994, operating under the Rent Control Ordinance, and its present regulations, it is entitled to earn a Net Operating Income of

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[12]*Baar, Guidelines For Drafting Rent Control Laws: Lessons of a Decade, 35 Rutg. L. Rev. 721* (1983).

$776,582[13] after *all* operating expenses (but not including debt service costs) are considered. This represents a "*fair and reasonable*" return when the full purchase price of the park is considered along with the Landlord's out-of-pocket investment. On the other hand, EL DORADO is contending that it is entitled to an additional rental increase which would allow it to "pass-through" its debt servicing cost as an additional expense. This is nonsense, and leads to the conclusion that EL DORADO seeks an unconscionable profit of $776,582 *AFTER* all expenses, including its debt service. Such a conclusion results in a return on investment of *555%*.[14] The *United States Constitution — Just Compensation Clause* — does NOT grant such a right to the Petitioner, EL DORADO.

IV.

DUE PROCESS RIGHTS — REGULATORY TAKING — JURISDICTION OF COMMISSION — RE: NON-DEBT SERVICE EXPENSES

EL DORADO's apparent attack on the COMMISSION's Ruling of October 30, 1991 (reaffirmed by the Trial Court and the Court of Appeals of the State of California)[15] completely ignores the uncontroverted fact that the COMMISSION has had *NO* subject matter jurisdiction to grant rent increases of "*indefinite*" *duration*. The COMMISSION's original ruling attempted to do this (indefinite duration — see EL DORADO's Petition, pg. 14 of App. 1) and, therefore, was void as to this subject matter (duration

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[13]EL DORADO's Base Year's (1982) NOI was established at $512,460. The current year's NOI is established by adjusting for CPI increases.

[14]EL DORADO's original investment was $140,000.

[15]See Appendix 1, from EL DORADO's Petition For Writ of Certiorari.

of increase). EL DORADO contended that the subject rent increase was a "*permanent*" increase, despite the fact that the COMMISSION's original ruling stated: "Said rent increase shall be effective September 1, 1988, and *continue until further order of this Commission.*" The ruling itself was totally void of any reference to "permanency." Accordingly, COMMISSION reassumed jurisdiction over the subject matter regarding the duration of any rent increase and rendered such decision on October 8, 1991.

The subject matter of "duration" concerned the entire rental increase not just that portion related to debt service expenses. The *entire* rental increase was of an *indefinite* duration. As such, the entire rental increase was subject to renewed jurisdiction by the COMMISSION to determine a proper duration (pursuant to its Rules/Regulations). The COMMISSION did assume subject matter jurisdiction regarding duration, and determined that the hardship rent increases (including non-debt service related increases) would expire on *June 1, 1993.*[16]

EL DORADO received the approximately $180.00 per month, per lot, rental increase for a period of 39 months — for the full duration of time in which the original promissory notes were in effect. Although such a rental increase was the result of an unconscionable loop-hole in the Ordinance, it was allowed to exist because EL DORADO acquired a vested right in acting *before* the Ordinance was amended. EL DORADO could have continued to receive the rental increase as long as it did not disturb the original financing. EL DORADO acted otherwise; its own conduct (100% refinancing) vitiated its right to continue to receive the rental increase. EL DORADO, therefore, has no claim against the COMMISSION for violating its alleged Consti-

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[16]Decision #8, pg. 8, COMMISSION's Findings & Decision of October 30, 1991.

tutional Rights. EL DORADO actually surrendered its rights by its own deliberate acts.

It is further interesting to note that since the date of the refinancing (March, 1989), to the present date, EL DORADO has filed *NO* "Hardship" rent increase request with the COMMISSION asserting that EL DORADO is not able to maintain its net operating income (NOI) along the guidelines of the *Ordinance*. EL DORADO's failure to seek administrative relief pursuant to the provisions of the *Ordinance* belies its claim that it is denied due process under the *Fifth and Fourteenth Amendments of the Constitution*. EL DORADO asserts a very weak argument, or excuse, that it has not done so (Hardship Application) because it takes too long and is costly, and that the possible benefit to be gained is far outweighed by such time and expense. How can EL DORADO claim a deprivation of due process when it itself waives its right to seek a remedy?

V.

CONCLUSION

The basic issue in this instance is not whether the *Ordinance* on-its-face, or as "applied," constitutes a regulatory taking of EL DORADO's property. As long as EL DORADO complied with the provisions and guidelines of the Ordinance, the facts in this instance clearly show that EL DORADO received "just compensation" — in the form of a "fair and reasonable" return on its investment. For a brief period of time (39 months), EL DORADO received an unconscionable return on its investment through the manipulation of a loop-hole in the provisions of the *Ordinance*. Upon the repeal of the loop-hole provisions (1986) and EL DORADO's subsequent acts for refinancing (1989), EL DORADO thus vitiated certain prior acquired rent increases. Nevertheless, subsequent to the date of refinancing, EL DORADO is still entitled to receive a "fair and reasona-

ble" return on its investment simply by seeking a hardship rent increase (from COMMISSION) to insure that it is able to maintain its net operating income. EL DORADO, by its own conduct and volition, has decided not to seek such a remedy. This Court should not assist the Petitioner in its own stubborn conduct; it already has a remedy available to it through an administrative process, a rent control "hardship" rent increase application. For the reasons stated hereinabove, the pending Petition For Writ of Certiorari should be denied.

Dated: November 10, 1994

Respectfully Submitted,

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